

Management Information Report
RRA Program Debt Recognition and Collection Experience
Report No. 01-09, July 26, 2001

This report presents the results of the Office of Inspector General's (OIG) study of Railroad Retirement Act (RRA) program debt recognition and collection experience at the Railroad Retirement Board (RRB).

BACKGROUND

The RRB is an independent agency in the executive branch of the Federal government. The RRB administers the health and welfare provisions of the RRA which provide retirement-survivor benefits for eligible railroad employees, their spouses, widows and other survivors. During fiscal year (FY) 2000, approximately 724,000 annuitants received benefits totaling \$8.3 billion under the RRA.

The RRB also administers the Railroad Unemployment Insurance Act (RUIA) which provides unemployment and sickness insurance to workers in the rail industry. During FY 2000, the RRB paid \$76.5 million to the 14,000 individuals qualifying for unemployment benefits and the 23,000 individuals qualifying for sickness benefits under the RUIA.

In FY 2000, the RRB established new accounts receivable due from the public totaling \$87.3 million including principal and interest. As of September 30, 2000, the agency reported outstanding receivables of \$51.8 million reduced by an allowance for doubtful accounts of \$12.5 million, or 24% of the total.

The debt recovery process begins with the recognition that a benefit overpayment has occurred. In many cases, notice of an event that will affect the benefit payment amount is received after-the-fact. If the corrected rate is lower than the amount actually paid in the past, the beneficiary will have been overpaid. The agency then recognizes a debt in its financial records and takes action to collect the overpayment.

The Bureau of Fiscal Operations has primary responsibility for the RRB's accounting operations. Within the Bureau of Fiscal Operations, the Debt Recovery Section (DRS) has overall responsibility for the RRB's debt collection activities, including monitoring the collection status of pending debt and pursuing delinquent debtors.

The Program Accounts Receivable (PAR) system is a mainframe computer application that supports the agency's debt recovery operations. It contains the detailed history of each debt recognized by the RRB including the cause, amount, collections, outstanding balance, and final disposition. Although DRS has administrative responsibility for the PAR system, the majority of transactions recorded in the PAR system are initiated in the Office of Programs.

This study addresses areas of management performance that support the RRB's strategic goal of safeguarding agency trust funds through prudent stewardship.

OBJECTIVE, SCOPE AND METHODOLOGY

The objective of this project was to identify relationships between the causes of overpayment and the effectiveness of the debt collection process. In order to accomplish our objective we:

- obtained a download of debt established during FY 1998 as of September 30, 1998, and updated the pending balance at the end of FY 1999, FY 2000 and March 2001;
- analyzed debt established during FY 1998 by cause of overpayment and status of collections;
- performed a limited review of the documentation supporting the PAR system entries for the 78 overpayments established during FY 1998 that exceeded \$25,000;
- interviewed agency management and staff concerning debt recognition and collection procedures; and
- obtained debt recovery statistics for prior years.

Fieldwork was conducted at RRB headquarters during February through May 2001.

RESULTS OF REVIEW

Our study of the RRB's debt recognition and collection experience shows a close relationship between the causes of RRA program overpayments and the outcome of the collection process. However, the inclusion of a high volume of non-debt transactions inflates reports of debt recognition and collection. The RRB established new receivables valued at \$87 million during FY 2000 of which approximately \$37 million (42%) is attributable to non-debt transactions.

In addition, current procedure does not provide for internal review or publication of measures of debt recovery performance, such as delinquency, turnover, clearance and cash collection rates that are traditionally used to evaluate the debt management function.

A detailed discussion of the results of our analysis follows.

RECOGNITION AND COLLECTION EXPERIENCE

Our study of the RRB's RRA debt recognition and collection experience shows rapid activity in clearing debt with a high percentage of debt clearances resulting from cash collections.

However, the RRB's experience in collecting overpayments attributable to the death of an annuitant or concurrent entitlement to Social Security benefits differs greatly from its experience with overpayments attributable to other causes.

In addition, the RRB maintains a large inventory of old, difficult to collect receivables that is offset by a large allowance for doubtful accounts.

Characteristics of RRA Program Debt

In order to extend our understanding of debt recognition and collection activity, we tracked the progress of the debt clearance process for RRA debts established during FY 1998.¹ We identified RRA debts that were recorded on the PAR system during FY 1998 and were still on the PAR system as of September 30 of that fiscal year.² At the end of FY 1999, FY 2000 and March 2001, we updated the outstanding balance for each debt in the population. In this manner, we were able to track the progress of the debt recovery process for a fixed population of receivables.

¹ Clearances include all transactions that reduce the balance of accounts receivable including collections, corrections, bad debt write-offs, and waivers of collection after due process.

² This population did not include debts that were declared erroneous and deleted from the PAR system prior to September 30, 1998.

Our analysis of PAR system data indicates that:

- individual debts are small, approximately 40% are under \$500, 90% are under \$2,000;
- more than 20% of the dollar value of debt established is concentrated in the 2% of overpayments that exceed \$5,000;
- the largest volume of debt clearances occur shortly after a debt is recognized with incremental reductions in the outstanding balances thereafter;
- cash collections represent no less than 90% of all debt clearances; and
- debt recovery experience varies widely by cause of overpayment.

RRA Debt Recovery Experience

As of September 30, 1998, the PAR system included RRA overpayments valued at over \$49 million that had been established during FY 1998 of which 77% had been cleared by the end of that fiscal year and nearly 90% was cleared during the next 12 months. The following table presents the long-term progress of debt clearances for accounts receivable established in FY 1998 by major cause of overpayment.

	Receivables <u>Established</u> (millions)	As of March 31, 2001	
		<u>Balance Outstanding</u> (millions)	<u>Percent Collected</u>
Benefits Released After the Death of an Annuitant	\$31.4	\$.8	98%
Concurrent Entitlement to Social Security Benefits	\$9.8	\$.4	95%
All Other Causes	8.3	\$ 2.2	74%
Total	\$49.5	3.4	93%

Incremental collections in all three categories, including “all other causes,” can be expected to continue. The RRB can expect to further reduce the balance of outstanding receivables by periodic withholding from the annuities of individuals with current or future entitlement to RRA benefits. In addition, the agency RRB may benefit from its participation in the inter-agency debt cross-servicing program coordinated by the U.S. Department of the Treasury (Treasury).

The high overall rate of clearances for debts resulting from the release of payments after the death of an annuitant and concurrent entitlement to Social Security benefits is due to the inclusion of some transactions that do not meet the definition of an account receivable.

RRA program debt recognized during FY 1998, detailed by cause of overpayment, is included as Appendix I to this report. A summary presentation of the collection experience of RRA program debt is presented in Appendix II.

Large Balance of Outstanding Receivables

The RRB's large balance of outstanding RRA and RUIA receivables (\$51.8 million at the end of FY 2000) and high allowance for doubtful accounts (\$12.5 million) is the result of its policy of maintaining an inventory of old, difficult to collect debt for up to 10 years. During that period, the RRB may be able to make incremental recoveries by withholding from future benefit entitlements and intra-governmental debt collection programs.

Unlike a private concern managing its trade receivables, the RRB cannot obtain any financial or business advantage by writing-off old debt.

NON-DEBT TRANSACTIONS INFLATE RECOGNITION AND COLLECTION DATA

The RRB's debt recognition and collection data are inflated by the inclusion of non-debt transactions.

The PAR system is used to account for returned and reclaimed benefit payments as well as certain transactions resulting from the coordination of RRA and Social Security benefits that do not meet the criteria for debt recognition. As a result, debt recognition and collection statistics that are prepared using PAR system data are inflated. In FY 2000, these three classes of transactions represented approximately \$37 million of the \$87 million in new debt recognized by the RRB.

Returned and Reclaimed Benefit Payments Are Recognized as Debt

Annuities are not payable under the Railroad Retirement Act for the month in which a beneficiary dies or any month thereafter. Such payments, whether issued by check or electronic funds transfer, must be returned to the RRB. In FY 2000, the RRB established approximately \$30 million in accounts receivable for benefit payments that were returned by individuals and financial institutions after the death of the annuitant.

Under current procedure, the RRB recognizes an account receivable for payments released after the death of an annuitant as soon as the agency is advised of the date of death. This practice is the result of procedural changes intended to enhance agency accountability for death-related debt. However, we believe returned payments and pending reclamations should not be recorded in the agency's accounting records as accounts receivable because they do not meet the criteria for receivable recognition.

In the Federal government a receivable should be recognized when a collecting entity establishes a specifically identifiable, legally enforceable claim to cash or other assets through its established assessment processes.³ Neither returned nor reclaimed payments meet this standard.

Returned Benefit Payments

In some cases, benefit payments released after the death of an annuitant are returned without a prior demand for repayment from the agency. Under current procedure, the RRB establishes an account receivable after the funds have been returned; no collection action is ever taken by the RRB.

A returned benefit payment does not meet the criteria for receivable recognition because it does not represent a claim to cash. The cash has already been received

³ Statements of Federal Financial Accounting Standards (SFFAS) Number 7, paragraph 53. This definition of accounts receivable from nonexchange transactions requires the standard for recognition of account receivable to be amended so that such receivables are not recognized on the basis of payment due dates but rather on the basis of the completion of the assessment processes.

and should be recognized in the agency's accounting records as a cash receipt rather than a receivable.

Reclaimed Benefit Payments

When the RRB is notified of the death of an annuitant, the agency terminates the payment of benefits effective with the month of death and establishes an account receivable. The agency initiates the Treasury reclamation process for any benefits released after the date of death.

The release of benefit payments in error is not sufficient to support recognition of an account receivable because it is based on due date alone. The party from whom the funds are to be recovered must also be identified. Until the reclamation process has been completed, the identity of the debtor against whom the Board can press a legal claim remains unknown.

Reclamation of benefit payments is literally a reversal of the original net payment transaction. Treasury demands return of the payment from the depositor's financial institution and credits the proceeds to the RRB. However, if checks have been negotiated or funds deposited electronically have been withdrawn, Treasury advises the agency of the name of the party receiving the funds. At that time, DRS takes the administrative action that is the basis for debt recognition: identification of a debtor, release of an overpayment letter and pursuit of collection.

Routine Social Security Adjustments Recognized as Debt

The RRB records an account receivable for all retroactive annuity adjustments resulting from concurrent entitlement to Social Security benefits, even when the RRB is immediately and fully reimbursed by withholding of accrued Social Security benefits. As a result, the RRB records approximately \$7 million per year more in debt and related collections than would otherwise be recognized.

The tier I portion of an RRA annuity must be reduced for any Social Security benefits that are concurrently payable. As a result of timing differences between the date of entitlement to concurrent benefits and notification to the RRB, reduction of the tier I benefit often requires a retroactive downward adjustment of the RRA annuity.

Under normal circumstances, retroactive downward adjustment of an annuity requires the RRB to seek return of the benefit overpayment from the annuitant. However, in order to facilitate the coordination of benefits between the two agencies, Congress has authorized the Social Security Administration to certify the Social Security benefits of Railroad Retirement annuitants to the RRB so that a single combined payment can be issued. In these cases, termed "LAF E Social Security cases," the retroactive payment of Social Security benefits becomes a paper transaction, in which the full amount of the tier I reduction for prior periods is withheld from the Social Security benefits that have

accrued unpaid for those periods.⁴ In most cases, there is never an outstanding balance to collect.

An account receivable recognizes a claim to cash or other assets; however, the retroactive adjustment that occurs when Social Security benefits are certified to the RRB for payment fully reimburses the RRB's trust funds. No claim to cash from the public exists. The RRB is effectively recognizing as debt transactions that were designed to prevent debt.

Non-Debt Transactions Distort Debt Recovery Statistics

In the discussion of debt recovery activity that accompanied the RRB's published financial statements, the agency reported establishing \$87 million in new receivables during FY 2000. Returned and reclaimed RRA benefit payments and retroactive adjustments to LAF E Social Security cases comprised approximately \$37 million (43%) of the total reported.

Inclusion of a high volume of non-debt transactions inflates the volume of program debt and presents an unnecessarily negative picture of the RRB's overall operations, distorts the relationship among data, and may obscure meaningful trends. In an analysis that excludes returned and reclaimed benefit payments and retroactive adjustments for LAF E Social Security entitlement, the dollar value of new debt would fall dramatically and the relative monetary impact of the various causes of overpayment would be altered.

In addition, inclusion of non-debt transactions in accounts receivable and debt recovery statistics can adversely impact the comparability of the RRB's experience with other entities. We compared the experience of the RRB as reported in the agency's financial statements with comparable data from the Social Security Administration for FY 1999.

The table below compares the debt recognition experience of the Social Security Old Age, Survivor and Disability (OASDI) programs with the comparable retirement and survivor programs of the RRA for FY 1999.

	OASDI	RRA
Benefit Payments	\$333.0 billion	\$8.0 billion
New Overpayments	\$ 2.3 billion	\$47.9 million
Overpayments Attributed to the death of the annuitant	\$ 94.0 million	\$31.5 million

In FY 1999, the Social Security Administration attributed new benefit overpayments of \$94 million to the release of payments after the death of the annuitant, approximately

⁴ The designation "LAF E" refers to the coding used in Social Security's master benefit record. "LAF E" benefits are paid by the Railroad Retirement Board. "LAF C" benefits are paid by the Social Security Administration.

4% of total OASDI debt detections. The RRB, a much smaller program, recognized \$31.5 million in death related-related receivables, approximately 65.8% of total RRA program debt. This difference in debt recognition experience between the two agencies is due to the Social Security Administration's limiting recognition of other death-related debt to payments that have not been successfully returned via the Treasury reclamation process.

Recommendations

We recommend that the Bureau of Fiscal Operations end the practice of recognizing a debt and related account receivable for:

1. returned benefit payments;
2. pending reclamations;
3. overpayments resulting from the retroactive downward adjustment of RRA annuities when recovery is simultaneously effected by withholding from accrued Social Security Benefits.

Management's Response

BFO management disagrees. BFO believes that the current agency process used for recognizing debt and related accounts receivable is appropriate and within the scope of the Statements of Federal Financial Accounting Standards (SFFAS) promulgated by the Federal Accounting Standards Advisory Board. They also believe that establishing accounts receivable for benefit payments issued after the death of the annuitant and overpayments resulting from Social Security adjustments provides effective management control because "these items can be recorded, compiled and tracked for management's analysis."

In support of their position BFO cited SFFAS No. 1, Accounting for Selected Assets and Liabilities, guidance obtained for preparing Treasury's Report on Receivables mandated by Treasury and draft guidance issued by the Joint Financial Management Improvement Program (JFMIP). Management also stated their belief that implementation of prior OIG audit recommendation had already ensured the adequacy of their current policy and procedure.

OIG'S Comments on Management's Response

We do not feel that BFO has made a convincing argument for rejection of the recommendations. The OIG continues to believe that the inclusion of returned benefit payments, pending reclamations and retroactive LAF E social security adjustments inflates the RRB's debt recognition and collection experience. Continued recognition of these transactions as debt will adversely impact the public perception of agency program performance and prevent meaningful comparisons with other entities.

BFO's response does not fully address the issues raised by the OIG's report. BFO has not offered a rationale for its policy of recognizing an account receivable *after cash has been returned* to the agency (returned benefit payments and retroactive LAF E Social Security adjustments) nor has it specifically explained why it believes that a pending reclamation requires debt recognition.

In addition, BFO has not addressed the lack of comparability between RRB and Social Security debt recognition experience as detailed in the report. Comparability is a significant issue that should be examined carefully. The divergence of the debt recognition experiences of the RRB and Social Security Administration has been raised by that agency as an obstacle to consideration of uncollected overpayments in the computation of the financial interchange between the two agencies, a change that can be expected to benefit the RRB.

BFO believes that establishing accounts receivable for returned and reclaimed benefit payments and LAF E Social Security adjustments provides effective management control because these items can be recorded, compiled and tracked for management's analysis. However, these transactions are also recorded in the agency's benefit payment systems. Even if the PAR system provides a more convenient repository for information about certain transactions, it is illogical to assume that all of those transactions must then be included in the agency's debt recognition and recovery statistics.

BFO cites the receivable standard set forth in SFFAS #1; however, they do not explain how that standard supports the recording of receivables *after the cash has been returned to the agency*. In addition, they do not acknowledge that the standard was amended by SFFAS #7 or their reasons for ignoring the amendment.

Treasury's satisfaction with BFO's method of preparing a special-use report, such as Treasury's Report on Receivables, is not pertinent to the present discussion. The issues raised in the OIG's report pertain to the perceptions of a much wider audience that includes both Federal and non-Federal users of financial information.

We must also note that Treasury has not mandated inclusion of all erroneous benefit payments for TROR reporting. According to BFO, Treasury's position is that "it is acceptable to establish erroneous benefit payments as receivables if we close them as either cancellations or adjustments." The OIG believes that the Treasury-approved policy of classifying returned benefit payments as "cancellations or adjustments," rather than "collections," supports the OIG's position that these transactions should never have been classified as receivables.

The JFMIP guidance cited by BFO is not relevant to the present discussion. The quoted passage states that receivables should be established but does not address the timing of debt recognition. BFO has not explained how the JFMIP guidance supports their position.

BFO cites two OIG audit reports to support their position, one of them was issued more than six years ago. Both reports focused on the functional implementation of existing agency policy. Neither report treated the high level issues examined in this report. The OIG reserves the right to re-visit any issue at any time.

AVAILABLE STATISTICS ARE NOT ADEQUATE FOR EVALUATION OF DEBT MANAGEMENT OPERATIONS

Debt recognition and collection statistics, as they are currently prepared and circulated, will not adequately support the program evaluation needs of higher levels of management.

The only widely circulated information concerning the RRB's debt recovery activity is presented in the agency's published financial statements and is limited to aggregate annual recognition and collection data supplemented by detail concerning the largest causes of overpayment and major methods of recovery. The Chief Financial Officer's monthly administrative report to the three-member Board includes only total receivables recognized and total recoveries recorded during the current month and the fiscal year to-date.

Establishment and review of performance measures and indicators are part of internal control. The limited information that is presently prepared and circulated does not provide meaningful information concerning the effectiveness and efficiency of the RRB's debt recovery operations because it does not include review or publication of key measures of debt management, such as delinquency, turnover, clearance and cash collection rates.

Recommendation

4. We recommend that the Bureau of Fiscal Operations, at least annually, prepare and circulate measures of debt recovery performance, such as delinquency, turnover, clearance and cash collection rates for use in evaluating the effectiveness and efficiency of debt recovery activities.

Management's Response

BFO concurs with the recommendation. BFO has agreed to report annually on key measures of debt management effectiveness and efficiency. This new procedure will supplement the debt recovery information that is currently prepared and circulated in connection with the agency's budget process, in BFO's monthly administrative reports and in response to special requests.